

**MAGNA WATER COMPANY,
AN IMPROVEMENT DISTRICT**

FINANCIAL STATEMENTS
with
INDEPENDENT AUDITORS' REPORTS
FOR THE YEAR ENDED DECEMBER 31, 2005

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees
Magna Water Company, an Improvement District
Magna, Utah

We have audited the accompanying basic financial statements of Magna Water Company, an Improvement District as of and for the year ended December 31, 2005, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Magna Water Company, an Improvement District as of December 31, 2005, and the results of its operations and the cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 18, 2006 on our consideration of Magna Water Company, an Improvement District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Management's Discussion and Analysis is not a required part of the financial statements, but is supplementary information the Governmental Accounting Standards Board requires. We applied limited procedures, consisting principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion thereon.

We performed our audit to form an opinion on the basic financial statements taken as a whole. The supplemental schedules listed in the Table of Contents are presented for additional analysis and are not a required part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Pinnock, Robbins, Posey & Richins

April 18, 2006

Management's Discussion and Analysis

As management of the Magna Water Company, an Improvement District, we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended December 31, 2005. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in the Independent Auditor's Report.

Financial Highlights

The assets of the District exceeded its liabilities at the close of the most recent fiscal year by \$33,936,439 (total net assets). Of this amount, \$6,916,638 (unrestricted net assets) may be used to meet the District's ongoing obligations to citizens and creditors.

The District's total net assets increased by \$3,126,773. Approximately 62% of this increase is attributable to water, sewer and secondary lines installed for new subdivisions then in turn contributed to the District. Other significant factors contributing to the increase include property taxes, interest income, and impact fees collected by new subdivisions.

At the end of the current fiscal year, unrestricted net assets were \$6,916,638 or 147% of total expenditures.

The District's total debt increased by \$10,523,090 (233%) during the current fiscal year. The key factor in this increase was due to the District bonding for the newly planned water treatment facility. The bonds in 2005 were general obligation bonds which were voted on in November of 2004 with a 71% approval rate.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves. The financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statement of revenues and expenses and changes in net assets presents information showing how the District's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

The District maintains one type of proprietary fund, an enterprise fund. A fund is a grouping of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The district, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the financial statements.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain supplementary information concerning the District's budget and actual amounts.

Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$33,936,439 at the close of the most recent fiscal year.

By far the largest portion of the District's net assets (66%) reflects its investment in capital assets (e.g., land, buildings, pipelines, machinery, and equipment); less any related debt used to acquire those assets that is still outstanding. The District uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Magna Water Company, an Improvement District Condensed Balance Sheet

	<u>2005</u>	<u>2004</u>
Current and other assets	\$ 23,418,452	\$ 11,079,961
Capital assets	<u>26,236,836</u>	<u>24,627,041</u>
Total Assets	<u>\$ 49,655,288</u>	<u>\$ 35,707,002</u>
Long-term liabilities outstanding	\$ 14,683,236	\$ 4,182,494
Other liabilities	<u>1,035,613</u>	<u>714,842</u>
Total Liabilities	<u>\$ 15,718,849</u>	<u>\$ 4,897,336</u>
Net Assets:		
Invested in capital assets, net of related debt	\$ 22,279,774	\$ 20,105,343
Restricted	4,740,027	4,354,306
Unrestricted	<u>6,916,638</u>	<u>6,350,017</u>
Total Net Assets	<u>\$ 33,936,439</u>	<u>\$ 30,809,666</u>

The restricted portion of the District's net assets (\$4,740,027) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets (\$6,916,638) may be used to meet the District's ongoing obligations to citizens and creditors.

There was an increase of \$385,721 in restricted net assets reported by the District. The increase resulted from a combination of an increase in the required replacement reserve account and collecting restricted impact fees.

The District's net assets increased by \$3,126,773 during the current fiscal year. About two thirds of this increase represents the degree of growth in the area. The increase is comprised of interest, impact fees collected and also the lines of which contractors have conveyed to the District. Approximately another third is attributable to the degree the District's operating and non-operating revenues have surpassed expenses for the year.

Magna Water Company, an Improvement District
Condensed Statement of Revenues, Expenses, and Changes in Net Assets

	2005	2004
Operating Revenues	\$ 3,805,731	\$ 4,000,124
Non-operating Revenues	<u>2,084,664</u>	<u>1,898,038</u>
Total Revenues	<u>5,890,395</u>	<u>5,898,162</u>
Depreciation and Amortization Expense	1,400,215	1,356,243
Other Operating Expense	3,005,498	2,894,918
Non-operating Expense	<u>303,959</u>	<u>149,578</u>
Total Expenses	<u>4,709,672</u>	<u>4,400,739</u>
Income before Capital Contributions	1,180,723	1,497,423
Capital Contributions	<u>1,946,050</u>	<u>57,836</u>
Change in Net Assets	3,126,773	1,555,259
Net Assets - Beginning of Year	<u>30,809,666</u>	<u>29,254,407</u>
Net Assets - Ending of Year	<u>\$ 33,936,439</u>	<u>\$ 30,809,666</u>

Major sources of revenue for the District consist of charges for services, property taxes, impact fees collected from new subdivisions, and new water and sewer lines installed by contractors and conveyed to the District. These sources account for 94% of the Districts revenues.

Total operating revenues were down by approximately 5% from the prior year, while total operating expenses were up by approximately 4%, leading to a decrease in income before capital contributions in 2005 as compared to the previous year. The capital contributions increased significantly in 2005 leading to an increase in net assets. The decrease in revenue is primarily due to a decrease in impact fees and development fees collected. The impact fees and development fees are collected in advance of the lines being contributed to the District, therefore, the increase or decrease in the impact fees and development fees do not always run parallel with the increase or decrease in the capital contributions. The increase in expenses is primarily due to inflation and growth in the demand of services for 2005.

Capital Asset and Debt Administration

Capital Assets. The District's investment in capital assets as of December 31, 2005 amounts to \$26,236,836 (net of accumulated depreciation). This investment in capital assets includes land, structures and improvements, wells and springs supply and transmission mains for water distribution and sewer collection, easements, water rights, construction in progress, plant and sewer systems, automobiles and equipment. The total increase in the District's investment in capital assets for the current fiscal year was approximately 7%. The District has been completing Phase I of the Secondary system. The reservoir was completed and filled during 2004, and the final stage of Phase I was bid and construction began in 2005. A new sludge handling process at the wastewater treatment plant was bid and construction began in 2005. Also, a new Special Improvement District was formed in West Valley City to install new water and sewer lines in the area of 5600 West, with the lines being conveyed to the District.

Capital Assets
Net of Accumulated Depreciation

	<u>2005</u>	<u>2004</u>
Land	\$ 933,695	\$ 642,436
Buildings and improvements	234,071	195,008
Water system	12,695,160	12,024,326
Secondary water system	155,682	—
Sewer treatment plant	5,502,853	5,839,251
Sewage collection lines	3,862,825	3,257,683
Machinery and equipment	288,175	387,335
Construction in progress	<u>2,564,375</u>	<u>2,239,453</u>
TOTAL	<u>\$ 26,236,836</u>	<u>\$ 24,585,492</u>

Additional information on the District's capital assets can be found in Note 3.

Long-term debt. At the end of the current fiscal year, the District had total long-term debt outstanding of \$15,044,788. Of this amount, \$3,110,000 is outstanding as revenue bond debt, \$1,084,788 relates to amounts outstanding on a water resource loan, and \$10,850,000 is outstanding as general obligation bonds.

Long-Term Debt

	<u>2005</u>	<u>2004</u>
General obligation bonds	\$ 10,850,000	\$ —
Revenue bonds	3,110,000	3,412,000
Water Resource Loan	<u>1,084,788</u>	<u>1,109,698</u>
	<u>\$ 15,044,788</u>	<u>\$ 4,521,698</u>

Additional information of the District's long-term debt can be found in Note 4.

Reserve Funds

The District held \$1,897,173 in reserves at the end of the current fiscal year. The reserve funds are mandatory by the revenue bonds.

Reserve and Fee Structure

In 2005 the District performed a rate study to determine the revenue requirements of the system based on the water and wastewater operations and capital facility needs. The District has implemented a three tier rate structure for the secondary system. The District anticipates the water and sewer user fees to increase in 2006.

Planned Future Capital Improvements

The District has initiated a secondary water system to serve the schools, parks, churches, and a new subdivision in the District's boundaries. Phase I of the secondary water project began in 2004 and was in operation in 2005. The secondary water reservoir was completed in 2004, and the final stage of Phase I of the secondary water system will be complete in 2006.

The District is in the preliminary design phase of a water treatment facility to comply with the federal mandate to treat drinking water for excess levels of arsenic. The District has to comply with the new MCL level of arsenic by January 2009. The new treatment plant is estimated to cost 21 million dollars to construct. The District is actively engaged in finding additional funding to assist in the cost. The District has currently issued \$10,850,000 in general obligation bonds for the project. There is also a 20-year master plan that the District follows to upgrade the water and sewer system to provide capacity needed for growth in the area.

The District is currently constructing a new sludge handling process at the wastewater treatment plant.

Requests for Information

This financial report is designed to provide a general overview of the District's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Magna Water Company, an Improvement District, Attention: District Manager, P.O. Box 303, Magna, Utah 84044.

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

BALANCE SHEET

DECEMBER 31, 2005

ASSETS

CURRENT ASSETS:

Cash and cash equivalents	\$ 6,658,209
Investments	141,606
Receivables:	
Property tax	59,524
Customers (less allowance for uncollectible accounts of \$2,075)	417,465
Other	142,754
Prepays	36,685
Inventories	203,886
Bond proceeds receivable	<u>5,000,000</u>

TOTAL CURRENT ASSETS 12,660,129

NONCURRENT ASSETS:

Restricted cash and cash equivalents	10,319,204
Restricted investments	245,363
Capital assets, net of accumulated depreciation	26,236,836
Deferred bond issuance costs, net of accumulated amortization of \$39,430	155,580
Water rights and shares	<u>38,176</u>

TOTAL NONCURRENT ASSETS 36,995,159

TOTAL ASSETS \$ 49,655,288

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES:

Accounts payable	\$ 282,898
Accrued liabilities	32,075
Compensated absences	75,894
Retainage payable	22,126
Accrued interest payable	261,068
Revenue bonds payable - current	319,000
Water Resource loan payable - current	<u>42,552</u>

TOTAL CURRENT LIABILITIES 1,035,613

NONCURRENT LIABILITIES:

General obligation bonds payable	10,850,000
Revenue bonds payable	2,791,000
Water Resource loan payable	<u>1,042,236</u>

TOTAL NONCURRENT LIABILITIES 14,683,236

TOTAL LIABILITIES 15,718,849

NET ASSETS:

Invested in capital assets, net of related debt	22,279,774
Restricted for:	
Debt service	1,899,318
Capital projects	2,840,709
Unrestricted	<u>6,916,638</u>

TOTAL NET ASSETS 33,936,439

TOTAL LIABILITIES AND NET ASSETS \$ 49,655,288

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

**STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS**

FOR THE YEAR ENDED DECEMBER 31, 2005

OPERATING REVENUES:	
Water sales	\$ 2,097,383
Sewer service charges	1,483,219
Connection fees and other income	<u>225,129</u>
TOTAL OPERATING REVENUES	<u>3,805,731</u>
OPERATING EXPENSES:	
Salaries and benefits	1,442,522
Contractual services	405,594
Materials and supplies	658,130
Utilities	266,833
Depreciation and amortization	1,400,215
Lease expense	28,245
Other operating expense	<u>204,174</u>
TOTAL OPERATING EXPENSES	<u>4,405,713</u>
OPERATING (LOSS)	<u>(599,982)</u>
NON-OPERATING REVENUES (EXPENSES):	
Property tax revenue	1,135,972
Non-resident fee in lieu of property taxes	47,747
Impact fees	470,182
Gain on sale of assets	3,746
Interest income	427,017
Interest expense	<u>(303,959)</u>
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>1,780,705</u>
INCOME BEFORE CAPITAL CONTRIBUTIONS	<u>1,180,723</u>
DEVELOPER CONTRIBUTED WATER AND SEWER LINES	<u>1,946,050</u>
CHANGE IN NET ASSETS	<u>3,126,773</u>
NET ASSETS AT BEGINNING OF YEAR	<u>30,809,666</u>
NET ASSETS AT END OF YEAR	<u>\$ 33,936,439</u>

See accompanying notes to the financial statements.

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED DECEMBER 31, 2005

CASH FLOWS FROM OPERATING ACTIVITIES:

Receipts from customers and users	\$ 3,735,818
Payments to suppliers	(1,492,606)
Payments to employees	<u>(1,439,848)</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES 803,364

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:

Property tax collected for maintenance and operations	<u>638,189</u>
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**NET CASH PROVIDED BY NONCAPITAL FINANCING
ACTIVITIES** 638,189

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING
ACTIVITIES:**

Receipts from impact fees	470,182
Property tax collected for debt service	500,000
Proceeds from capital debt	5,941,090
Purchases of capital assets	(1,087,944)
Principal paid on capital debt	(418,000)
Interest paid on capital debt	(125,979)
Payment of bond issuance costs	(154,379)
Proceeds from sale of capital assets	<u>3,746</u>

**NET CASH PROVIDED BY CAPITAL AND RELATED
FINANCING ACTIVITIES** 5,128,716

CASH FLOWS FROM INVESTING ACTIVITIES:

Purchase of investments	(18,203)
Interest received	<u>427,017</u>

NET CASH PROVIDED BY INVESTING ACTIVITIES 408,814

NET INCREASE IN CASH AND CASH EQUIVALENTS 6,979,083

CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR 9,998,330

CASH AND CASH EQUIVALENTS, END OF YEAR \$ 16,977,413

CASH APPEARS ON THE BALANCE SHEET AS FOLLOWS:

Cash and cash equivalents - unrestricted	\$ 6,658,209
Cash and cash equivalents - restricted	<u>10,319,204</u>

\$ 16,977,413

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

STATEMENT OF CASH FLOWS (CONTINUED)

FOR THE YEAR ENDED DECEMBER 31, 2005

**RECONCILIATION OF OPERATING (LOSS) TO NET CASH
PROVIDED BY OPERATING ACTIVITIES:**

Operating (loss)	\$ (599,982)
Adjustments to reconcile operating (loss) to net cash provided by operating activities:	
Depreciation and amortization	1,400,215
Changes in operating assets and liabilities:	
(Increase) decrease in:	
Receivables	(89,033)
Prepays	19,120
Inventories	(50,772)
Water rights and shares	3,373
Increase (decrease) in:	
Accounts payable	106,646
Accrued liabilities	(11,003)
Compensated absences	2,674
Retainage payable	<u>22,126</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES \$ 803,364

**NONCASH INVESTING, CAPITAL, AND FINANCING
ACTIVITIES:**

The District received water and sewer lines from subdividers in the amount of \$1,946,050 in 2005, which represent the fair value of lines deeded to the District. These additions are accounted for as capital contributions in the statement of revenues, expenses, and changes in net assets.

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

Magna Water Company, an Improvement District, is a special district governed by an elected three member board. Generally accepted accounting principles require that these financial statements present the government and its component units, entities for which the government is considered to be financially accountable. The District was created July 7, 1949 by a resolution of the Board of County Commissioners of Salt Lake County. Salt Lake County has no oversight responsibility over the District and the District is not reported as a component unit of Salt Lake County. The District has no blended or discretely presented component units.

B. Measurement Focus and Basis of Accounting

The District is an enterprise fund, which is reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the proprietary fund financial statements to the extent that those standards do not conflict with or contradict the guidance of the Governmental Accounting Standards Board. Governments also have the *option* of following subsequent private-sector guidance for their enterprise funds, subject to the same limitation. The government has elected not to follow subsequent private-sector guidance.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the District are charges to customers for water and sewer services. Operating expenses include the costs of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources as they are needed.

C. Budgetary Procedures and Budgetary Accounting

Budgetary procedures for the Agency have been established by the Uniform Fiscal Procedures Act adopted by the State of Utah, which requires the legal adoption of a budget for all funds. Furthermore, in accordance with state law, all appropriations lapse at the end of the budget year; accordingly, no encumbrances are recorded. The basis of accounting applied to the budget is that same basis as the financial statements.

A formal budget has been adopted and used as a control device during the year ended December 31, 2005.

No budget is required to be presented in these financial statements. State law allows the District to amend the proprietary fund budget without public hearing or public notice.

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Budgetary Procedures and Budgetary Accounting (continued)

The District follows the following procedures in its budgetary process:

1. During October or November of each year the District adopts a tentative annual budget for the upcoming calendar year.
2. The tentative budget is a public record and is available for public inspection.
3. At least ten days prior to the second Tuesday in November of each year, the District publishes a notice of public hearing in an issue of a newspaper of general circulation for the purpose of adopting the budget.
4. On the second Tuesday in November, the budget is formally adopted after consideration of public comment.

D. Cash and Cash Equivalents

The District considers all highly liquid investments with a maturity of three months or less when purchased to be "cash equivalents".

E. Deferred Bond Issuance Costs

Costs incurred related to the issuance of bonds are deferred and amortized over the term of the related bonds using the straight line method.

F. Inventories

The District maintains inventories of pipe, repair parts, hydrants, and water meters. Inventories are stated at lower of cost or market using the first in/first out (FIFO) method.

G. Capital Assets

Capital assets include land, building and improvements, water and sewer systems, and machinery and equipment. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful live in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period. No interest was capitalized during the current fiscal year.

Property, plant, and equipment of the District is depreciated using the straight line method over the following estimated useful lives:

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. Capital Assets (continued)

Water utility plant	20 to 50 years
Sewer utility plant	30 to 50 years
Buildings and structures	30 to 40 years
Equipment	3 to 15 years
Furniture and fixtures	5 to 10 years

H. Employee Benefits and Compensated Absences

The District provides pension, medical, dental, vision, and life insurance to its employees, all of which are negotiated by contract with the Teamsters Union. Employees are also provided paid holidays and vacation pay, which does not accumulate from year to year, but a maximum of 80 hours can be cashed out at the end of each year. Sick leave accumulates at a rate of one-half day per month and can be carried over from year to year without limitation.

I. Property Tax Revenues

Property taxes are levied on January 1st based on the assessed values of property listed on the previous May 31st. Assessed values are an approximation of market value. Property taxes become delinquent after November 30. The District's tax rate for 2005 was .001502, which is comprised of .000713 for operations and maintenance and .000789 for debt service. The statutory maximum set by the state for operations and maintenance is .000800. There is no statutory maximum for the reduction of general obligation bonds.

J. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the District to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

2. DEPOSITS AND INVESTMENTS

Deposits and investments for local government are governed by the Utah Money Management Act (*Utah Code Annotated*, Title 51, Chapter 7, "the Act") and by rules of the Utah Money Management Council ("the Council"). Following are discussions of the District's exposure to various risks related to its cash management activities.

A. Deposits

	<u>Bank Balances</u>	<u>Book Balances</u>
Cash on hand	\$ —	\$ 1,300
Cash on deposit	<u>564,701</u>	<u>365,035</u>
TOTAL	<u>\$ 564,701</u>	<u>\$ 366,335</u>

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

2. DEPOSITS AND INVESTMENTS (CONTINUED)

A. Deposits (continued)

Custodial Credit Risk: Custodial credit risk is the risk that, in the event of a bank failure, the District's deposits may not be recovered. The District's policy for managing custodial credit risk is to adhere to the Money Management Act. The Act requires all deposits of the District to be in a *qualified depository*, defined as any financial institution whose deposits are insured by an agency of the federal government and which has been certified by the Commissioner of Financial Institutions as meeting the requirements of the Act and adhering to the rules of the Utah Money Management Council. As of December 31, 2005, \$463,701 of the district's bank balance of \$564,701 was uninsured and uncollateralized.

B. Investments

Credit Risk: Credit risk is the risk that the counterparty to an investment will not fulfill its obligations. The District's policy for limiting the credit risk of investments is to comply with the Money Management Act. The Act requires investments transactions to be conducted only through qualified depositories, certified dealers, or directly with issuers of investment securities. Permitted investments include deposits of qualified depositories; repurchase agreements; commercial paper that is classified as "first tier" by two nationally recognized statistical rating organizations, one of which must be Moody's Investors Services or Standard & Poor's; bankers' acceptances; obligations of the U.S. Treasury and U.S. government sponsored enterprises; bond and notes of political subdivisions of the State of Utah; fixed rate corporate obligations and variable rate securities rated "A" or higher by two nationally recognized statistical rating organizations as defined in the Act.

The District is authorized to invest in the Utah Public Treasurer's Investment fund (PTIF), as external pooled investment fund managed by the Utah State Treasurer and subject to the Act and Council requirements. The PTIF is not registered with the SEC as an investment company, and deposits in the PTIF are not insured or otherwise guaranteed by the State of Utah. The PTIF operates and reports to participants on an amortized cost basis. The income, gains, and losses, net of administration fees, of the PTIF are allocated based upon the participants' average daily balance.

As of December 31, 2005, the District had the following investments and maturities:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (in Years)</u>			
		<u>Less Than 1</u>	<u>1-5</u>	<u>6-10</u>	<u>More Than 10</u>
Money Market Funds	\$ 1,601,447	\$ 1,601,447	\$ -	\$ -	\$ -
Grand Cayman	3,399,312	3,399,312	-	-	-
Certificates of deposit	386,969	-	386,969	-	-
State of Utah Public Treasurer's Investment Fund	<u>11,610,319</u>	<u>11,610,319</u>	<u>-</u>	<u>-</u>	<u>-</u>
TOTAL	<u>\$ 16,998,047</u>	<u>\$ 16,611,078</u>	<u>\$ 386,969</u>	<u>\$ -</u>	<u>\$ -</u>

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The District manages its exposure to declines in fair value by investing mainly in the PTIF and by adhering to the Money Management Act. The Act requires that the remaining term to maturity of investments may not exceed the

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

2. DEPOSITS AND INVESTMENTS (CONTINUED)

B. Investments (continued)

period of availability of the funds to be invested. The Act further limited the remaining term to maturity of commercial paper to 270 days or less and fixed rate negotiable deposits and corporate obligations to 365 days or less. Maturities of the District's investments are noted above.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The District's policy to reduce this risk is to adhere to the rules of the Money Management Council. The Council's Rule 17 limits investments in a single issuer of commercial paper and corporate obligations to between five and ten percent depending upon the total dollar amount held in the District's portfolio at the time of purchase.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The District does not have a formal policy for custodial credit risk.

3. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2005 was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
CAPITAL ASSETS NOT BEING DEPRECIATED:				
Land	\$ 642,436	\$ 291,259	\$ -	\$ 933,695
Construction in progress	<u>2,239,453</u>	<u>330,828</u>	<u>(5,906)</u>	<u>2,564,375</u>
Total Capital assets, not being depreciated	<u>2,881,889</u>	<u>622,087</u>	<u>(5,906)</u>	<u>3,498,070</u>
CAPITAL ASSETS, BEING DEPRECIATED:				
Buildings and improvements	424,886	57,098	-	481,984
Water system	20,044,622	1,338,330	(100)	21,382,852
Secondary water system	-	158,638	-	158,638
Sewer treatment plant	10,482,826	28,399	-	10,511,225
Sewage collection lines	6,397,053	798,584	-	7,195,637
Machinery and equipment	<u>1,773,266</u>	<u>36,764</u>	<u>-</u>	<u>1,810,030</u>
Total capital assets being depreciated	<u>39,122,653</u>	<u>2,417,813</u>	<u>(100)</u>	<u>41,540,366</u>
LESS ACCUMULATED DEPRECIATION FOR:				
Buildings and improvements	(229,878)	(18,035)	-	(247,913)
Water system	(8,020,296)	(667,496)	100	(8,687,692)
Secondary water system	-	(2,956)	-	(2,956)
Sewer treatment plant	(4,643,575)	(364,797)	-	(5,008,372)
Sewage collection lines	(3,139,370)	(193,442)	-	(3,332,812)
Machinery and equipment	<u>(1,385,931)</u>	<u>(135,924)</u>	<u>-</u>	<u>(1,521,855)</u>
Total accumulated depreciation	<u>(17,419,050)</u>	<u>(1,382,650)</u>	<u>100</u>	<u>(18,801,600)</u>
Total capital assets, being depreciated, net	<u>21,703,603</u>	<u>1,035,163</u>	<u>-</u>	<u>22,738,766</u>
CAPITAL ASSETS, NET	<u>\$24,585,492</u>	<u>\$ 1,657,250</u>	<u>\$ (5,906)</u>	<u>\$26,236,836</u>

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

4. LONG-TERM DEBT

General Obligation Bonds

The District issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities. There were no general obligation bonds issued in prior years. During the year, general obligation bonds totaling \$10,850,000 were issued to provide funds for the construction of a water treatment plant.

General obligation bonds are direct obligations and pledge the full faith and credit of the District. General obligation bonds currently outstanding are as follows:

<u>Purpose</u>	<u>Interest Rates</u>	<u>Amount</u>
Water treatment plant	2.27%	\$ 6,000,000
Water treatment plant	4.43 – 5.12%	<u>4,850,000</u>
		<u>\$10,850,000</u>

Annual debt service requirements to maturity for general obligation bonds are as follows:

<u>Year Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt Service</u>
2006	\$ —	\$ 329,774	\$ 329,774
2007	240,000	369,068	609,068
2008	846,000	357,086	1,203,086
2009	876,000	324,403	1,200,403
2010	912,000	289,667	1,201,667
2011-2015	4,346,000	851,662	5,197,662
2016-2020	1,540,000	343,678	1,883,678
2021-2025	1,722,000	160,785	1,882,785
2026-2030	<u>368,000</u>	<u>8,354</u>	<u>376,354</u>
TOTAL	<u>\$ 10,850,000</u>	<u>\$ 3,034,477</u>	<u>\$ 13,884,477</u>

Revenue Bonds

The District also issues bonds where the District pledges income derived from the acquired or constructed assets to pay debt service. The original amount of revenue bonds issued in prior years was \$4,870,000. No revenue bonds were issued during the current year. Revenue bonds outstanding at year end are as follows:

<u>Purpose</u>	<u>Interest Rates</u>	<u>Amount</u>
Water facilities	2.93%	713,000
Water facilities	3.00%	911,000
Water facilities	5.15 – 5.60%	244,000
Sewer facilities	3.50%	<u>1,242,000</u>
		<u>\$ 3,110,000</u>

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

4. LONG-TERM DEBT (CONTINUED)

Annual debt service requirements to maturity for revenue bonds are as follows:

<u>Year Ending</u> <u>December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt</u> <u>Service</u>
2006	\$ 319,000	\$ 421,023	\$ 740,023
2007	336,000	424,623	760,623
2008	293,000	371,206	664,206
2009	308,000	376,810	684,810
2010	323,000	381,940	704,940
2011-2015	1,025,000	1,159,538	2,184,538
2016-2020	506,000	517,193	1,023,193
TOTAL	<u>\$ 3,110,000</u>	<u>\$ 3,652,333</u>	<u>\$ 6,762,333</u>

Water Resource Loan

The District has entered into an agreement with the State of Utah Division of Water Resources (State) for the construction of a secondary water system. Under this agreement, the State has agreed to advance to the District, at an annual interest rate of 1.00%, up to \$1,175,000 to fund construction on the project. As of December 31, 2005, total amounts advanced by the State were \$1,175,000, and amounts outstanding were \$1,084,788.

Annual debt service requirements to maturity for the Water Resource Loan are as follows:

<u>Year Ending</u> <u>December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt</u> <u>Service</u>
2006	\$ 42,552	\$ 10,848	\$ 53,400
2007	42,978	10,422	53,400
2008	43,407	9,993	53,400
2009	43,841	9,559	53,400
2010	44,280	9,120	53,400
2011-2015	228,131	38,869	267,000
2016-2020	239,768	27,232	267,000
2021-2025	251,998	15,002	267,000
2026-2030	147,833	2,872	150,705
TOTAL	<u>\$ 1,084,788</u>	<u>\$ 133,917</u>	<u>\$ 1,218,705</u>

Changes in Long-Term Debt

Long-term debt activity for the year ended December 31, 2005 was as follows:

	<u>Beginning</u> <u>Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending</u> <u>Balance</u>	<u>Due Within</u> <u>One Year</u>
Bonds payable:					
General obligation bonds	\$ —	\$10,850,000	\$ —	\$10,850,000	\$ —
Revenue bonds	3,412,000	—	302,000	3,110,000	319,000
Total bonds payable	3,412,000	10,850,000	302,000	13,960,000	319,000
Water resource loan	1,109,698	91,090	116,000	1,084,788	42,552
TOTAL LONG-TERM DEBT	<u>\$ 4,521,698</u>	<u>\$10,941,090</u>	<u>\$ 418,000</u>	<u>\$15,044,788</u>	<u>\$ 361,552</u>

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

5. RESERVE REQUIREMENTS OF THE 1994 SEWER REVENUE BOND RESOLUTIONS

The District is required to establish three reserve accounts to provide for proper servicing of the 1994 Revenue Bond and repairs and replacement of the treatment facility as considered necessary. Following is a description of these reserve accounts.

Bond and Hardship Grant Assessment Account

This account is to assure the "prompt payment of the Series 1994 Bonds and Hardship Grant Assessment as it becomes due". The amount set aside and allocated each month should be 1/12 of the principal and interest due the succeeding year.

Reserve Account

The District is also required to make monthly contributions to a Reserve Account to be used to pay the principal falling due on the 1994 Bonds at any time when there are not sufficient funds in the Bond and Hardship Assessment Account to pay the same. Required monthly contributions to this Reserve Account are \$2,275 until the account balance reaches \$163,785.

Emergency Reserve Account

In like manner, the District is also required to make a monthly contribution to an Emergency Repair and Replacement Account. The monthly contribution is \$1,137 plus such additional amounts as may be required to meet any monthly installment to said account which has not been previously paid. These contributions are to continue until the account has accumulated \$81,893.

Required reserve fund balances as of December 31, 2005 are as follows:

	<u>Amount Required</u>	<u>Amount on Deposit</u>
Bond and Hardship grant assessment account:		
Amounts allocated to principal	\$ 120,000	\$ 120,000
Amounts allocated to interest	<u>43,470</u>	<u>43,470</u>
TOTAL	<u>\$ 163,470</u>	<u>\$ 163,470</u>
Reserve account	\$ 163,785	\$ 163,470
Emergency reserve account	<u>81,893</u>	<u>81,893</u>
TOTAL RESERVE REQUIREMENTS	<u>\$ 245,678</u>	<u>\$ 245,363</u>

The District maintains control of these accounts. However, withdrawals from these accounts are not allowed except for purposes stated in the 1994 Bond and Hardship Grant agreement.

6. RESERVE REQUIREMENTS OF THE 1997 WATER REVENUE BOND RESOLUTIONS

The District is required to establish four reserve accounts to provide for proper service of the 1997 Revenue Bonds and replacement of the treatment facility as considered necessary. Following is a description of these reserve accounts.

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

6. RESERVE REQUIREMENTS OF THE 1997 WATER REVENUE BOND RESOLUTIONS (CONTINUED)

Debt Service Reserve Account

The District is required to make monthly contributions to Debt Service Reserve Accounts, for each of the 1997 Water Revenue Bonds, to be used to pay principal falling due on the 1997 Bonds at any time when there are not sufficient funds to pay the same. Annual contributions to these Reserve Accounts are required until the account balance reaches \$67,218, \$100,000 and \$100,000 for the 1997 A, B and C Bonds respectively.

Replacement Account

In like manner, the District is also required to make an annual contribution to a Replacement Account. The annual contribution is 5% of the annual water operating budget, including debt service and depreciation, and must continue until the 1997 A Bond is redeemed.

Required reserve fund balances as of December 31, 2005 are as follows:

	<u>Amount Required</u>	<u>Amount on Deposit</u>
Reserve accounts	\$ 522,390	\$ 522,390
Replacement account	<u>965,635</u>	<u>965,635</u>
TOTAL RESERVE REQUIREMENTS	<u>\$1,488,025</u>	<u>\$ 1,488,025</u>

7. EMPLOYEES PENSION PLAN

All full-time District employees are members of the Western Conference of Teamsters Pension Trust fund, a multiple employer union plan, under a current collective bargaining agreement covering the period June 1, 2002 through May 31, 2006. The District makes pension contributions to the Pension Trust fund, a defined benefit pension plan, on behalf of all employees at the rate of \$3.49 per hour.

District contributions to the Trust Fund were \$142,710, \$153,816 and \$148,225 for 2005, 2004 and 2003, respectively.

8. POST-RETIREMENT HEALTHCARE BENEFITS

In accordance with the Union contract, the District provides post-retirement healthcare benefits to all eligible retired employees. Expenditures amounted to \$25,347 for 2005.

9. COMMITMENTS

The District has entered into an agreement with the Jordan Valley Water Conservancy District to purchase a minimum of 800 acre feet of water annually. During the year ended December 31, 2005 the District purchased 928 acre feet, at a cost of \$214,037.

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

9. COMMITMENTS (CONTINUED)

During the year, the District entered into contracts for construction of secondary water and sewer facilities. As of December 31, 2005, there was approximately \$1,259,000 outstanding on the contracts.

10. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omission; and natural disasters for which the District insures with the Local Government Trust Risk Pool.

11. CONTINGENCIES

Contamination of the groundwater aquifer by perchlorate, a potentially hazardous substance leaked into the groundwater by private industry and the federal government, is being studied and closely monitored by the District and the private industrial firm currently involved. The private firm has been paying a portion of the District's costs of these efforts. The District and the firm entered into an agreement in December 2004 concerning the removal of perchlorate from water produced by three of the District's wells. Under the agreement, the firm will pay for a substantial portion of a new treatment facility proposed by the District and for a portion of the operation and maintenance of that facility. The District is issuing bonds to finance this treatment facility. The agreement has a provision for a partial refund to the firm if future perchlorate standards merit such a refund. There is also a limited waiver of liability for the firm, subject to the terms and conditions of the agreement.

During the year ended December 31, 2005, the District issued general obligation bonds totaling \$10,850,000 to fund water treatment facilities. The District is actively engaged in finding additional funding to comply with the federal mandate to treat drinking water for excess levels of arsenic. The District received an extension to comply with the new MCL level of arsenic by January 2009.

The District anticipates that costs associated with a new water treatment plan which will facilitate the removal of perchlorate and lower arsenic levels to the required standards will approximate \$21 million.

SUPPLEMENTAL SCHEDULES

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT**SCHEDULE OF REVENUES AND EXPENSES**
AND CHANGES IN NET ASSETS**FOR THE YEAR ENDED DECEMBER 31, 2005****OPERATING REVENUES:**

Charges for services:

Water sales	\$ 2,097,383
Sewer service charges	1,483,219
Connection fees and other income	<u>225,129</u>
	<u>3,805,731</u>

OPERATING EXPENSES:

Salaries and benefits:

Salaries and wages – plant	720,342
Salaries and wages – office	241,791
Trustees' salaries	7,500
Payroll taxes and union fringe benefits	<u>472,889</u>
	<u>1,442,522</u>

Contractual services:

Legal	67,151
Lobbyist fees	50,000
Accounting	33,750
Engineering	148,729
Data processing services	12,497
Janitorial	6,240
Lab and testing	<u>87,227</u>
	<u>405,594</u>

Lease expense	<u>28,245</u>
---------------	---------------

Materials and supplies:

Repairs, maintenance and supplies	366,205
Office supplies and postage	77,888
Water purchased	<u>214,037</u>
	<u>658,130</u>

Utilities:

Electricity and fuel for water production and sewer processing	239,652
Office and general, electricity and fuel	5,952
Telephone and paging	<u>21,229</u>
	<u>266,833</u>

Depreciation and amortization	<u>1,400,215</u>
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Other operating expenses:

Transportation	53,292
Bad debts	7,251
Insurance	71,805
Training	30,946
Miscellaneous	<u>40,880</u>
	<u>204,174</u>

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT**SCHEDULE OF REVENUES AND EXPENSES**
AND CHANGES IN NET ASSETS (CONTINUED)**FOR THE YEAR ENDED DECEMBER 31, 2005**

TOTAL OPERATING EXPENSES	<u>\$ 4,405,713</u>
OPERATING (LOSS)	<u>(599,982)</u>
NON-OPERATING REVENUES (EXPENSES):	
Property tax revenue	1,135,972
Non-resident fee in lieu of property taxes	47,747
Impact fees	470,182
Gain on sale of assets	3,746
Interest income	427,017
Interest expense	<u>(303,959)</u>
NET NON-OPERATING REVENUES	<u>1,780,705</u>
DEVELOPER CONTRIBUTED WATER AND SEWER LINES	<u>1,946,050</u>
CHANGE IN NET ASSETS	<u>\$ 3,126,773</u>

MAGNA WATER COMPANY, AN IMPROVEMENT DISTRICT**SCHEDULE OF REVENUES AND EXPENSES**
AND CHANGES IN NET ASSETS
COMPARED WITH BUDGET**FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>Approved Budget</u>	<u>Actual</u>	<u>Difference Favorable (Unfavorable)</u>
OPERATING REVENUES:			
Water sales	\$ 2,200,000	\$ 2,097,383	\$ (102,617)
Sewer service charges	1,500,000	1,483,219	(16,781)
Connection fees and other income	397,000	225,129	(171,671)
	<u>4,097,000</u>	<u>3,805,731</u>	<u>(291,069)</u>
OPERATING EXPENSES:			
Salaries and benefits	1,739,500	1,442,522	296,978
Contractual services	354,800	405,594	(50,794)
Materials and supplies	792,500	658,130	134,370
Utilities	345,200	266,833	78,367
Depreciation and amortization	1,627,800	1,400,215	227,585
Lease expense	29,000	28,245	755
Other operating expense	290,800	204,174	86,626
	<u>5,179,600</u>	<u>4,405,713</u>	<u>773,887</u>
NON-OPERATING REVENUE:			
Property tax revenue	1,003,513	1,135,972	132,459
Non-resident fee in lieu of property taxes	47,000	47,747	747
Gain on disposal of assets	2,500	3,746	1,246
Impact fees	650,000	470,182	(179,818)
Interest income	90,000	427,017	337,017
	<u>1,793,013</u>	<u>2,084,664</u>	<u>291,651</u>
NON-OPERATING EXPENSE:			
Interest expense	133,000	303,959	(170,959)
	<u>133,000</u>	<u>303,959</u>	<u>(170,959)</u>
INCOME BEFORE CAPITAL CONTRIBUTIONS	<u>577,413</u>	<u>1,180,723</u>	<u>603,310</u>
DEVELOPER CONTRIBUTED WATER AND SEWER LINES	<u>920,000</u>	<u>1,946,050</u>	<u>1,026,050</u>
CHANGE IN NET ASSETS	<u>\$ 1,497,413</u>	<u>\$ 3,126,773</u>	<u>\$ 1,629,360</u>



PINNOCK, ROBBINS, POSEY & RICHINS

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Trustees
Magna Water Company, an Improvement District
Magna, Utah

We have audited the financial statements of Magna Water Company, an Improvement District, as of and for the year ended December 31, 2005, and have issued our report thereon dated April 18, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Magna Water Company's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control over Financial Reporting

In planning and performing our audit, we considered Magna Water Company's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of Magna Water Company's management, Board of Trustees, and applicable federal and state agencies. It is not intended to be and should not be used by anyone other than these parties.

Pinnock, Robbins, Posey & Richins

April 18, 2006



PINNOCK, ROBBINS, POSEY & RICHINS

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INDEPENDENT AUDITORS' REPORT ON STATE LEGAL COMPLIANCE

Board of Trustees
Magna Water Company, an Improvement District
Magna, Utah

We have audited the accompanying basic financial statements of Magna Water Company, an Improvement District for the year ended December 31, 2005 and have issued our report thereon dated April 18, 2006.

Our audit included test work on the District's compliance with the following general compliance requirements identified in the State of Utah Legal Compliance Audit Guide:

Public Debt	Truth in Taxation and Property Tax Limitations
Cash Management	Special Districts
Budgetary Compliance	Other General Issues
Purchasing Requirements	Impact Fees

The District did not receive any major or non-major State Grants during the year ended December 31, 2005.

The management of Magna Water Company, an Improvement District is responsible for the District's compliance with all compliance requirements identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed immaterial instances of noncompliance with the requirements referred to above, which are described in the accompanying management letter. We considered these instances of non-compliance in forming our opinion on compliance, which is expressed in the following paragraph.

In our opinion, Magna Water Company, an Improvement District, complied, in all material respects, with the general compliance requirements identified above for the year ended December 31, 2005.

Pinnock, Robbins, Posey & Richins

April 18, 2006



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April 18, 2006

To the Board of Trustees
Magna Water Company, An Improvement District

Dear Members:

We have completed our audit of Magna Water Company, an Improvement District (the District) for the year ended December 31, 2005. The District is ultimately responsible for the financial condition of the District, and for the District's compliance with finance related state and federal law. The Uniform Fiscal Procedures Act outlines responsibilities of the governing body.

The purpose of the financial statements is to report in summary form, the financial condition of the District, and the results of its operations and changes in financial condition, and to provide information to the governing body to help them satisfy their legal and political responsibilities for determining and demonstrating compliance with the various finance related state and federal law.

During our audit, we noted various matters involving the internal control structure and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve the internal control structure or result in other operating efficiencies and are summarized as follows:

STATE LEGAL COMPLIANCE

CERTIFICATION REQUIREMENTS

Finding (prior year recommendation)

State legal compliance requirements include the requirement for the district to certify annually to the county treasurer, in writing, that the required listing information has been provided to the local telephone directory publisher. This certification was not provided to the county in 2004.

Recommendation

We recommend that the District comply with the certification requirements to the county regarding listing information with the local telephone directory publisher.

Management's Response

This recommendation was given after the June 30, 2005 certification deadline; therefore, although the District was not compliant for 2005, as of the date of this report, the required information has been published in the local telephone directory and the County has been notified.

CASH MANAGEMENT

Finding (prior year recommendation)

We noted during our audit that one of the daily cash deposits tested was not deposited within three business days, as required by Utah State law.

Recommendation

We recommend that all deposits be made within at least three business days.

Management's Response

The District has introduced new staff and procedures to the cash deposit process. Significant improvement has been made in this area, and the auditors have noted only one violation to the three day deposit requirement since our prior year recommendation was received. Management is aware of the violation, and is committed to complying with this requirement.

PURCHASING POLICY

Finding (prior year recommendation)

We noted during our audit that certain purchases did not have the required signed approvals, as required by the District's purchasing policy. Utah State law requires that all purchases of the District be made according to the established purchasing policy.

Recommendation

We recommend that the District comply with its purchasing policy requiring signed approvals.

Management's Response

Significant improvement has been made in this area. The auditors found only one exception where a disbursement was made without a properly signed request form. Management is aware of this exception, and is committed to complying with this requirement.

CASH RECEIPTS

Finding

We noted during our audit that the individual responsible for reviewing and signing off on daily balancing sheets did not have oversight on her own daily balancing sheet. Proper review and oversight is necessary on the daily balancing sheet for all cash tills to provide the level of control necessary to prevent potential misappropriation and misstatement.

Recommendation

We recommend that all cash tills and daily balancing sheets be properly reviewed.

Management's Response

Management will comply.

CASH DISBURSEMENTS

Finding (prior year recommendation)

We noted during our audit that one of the disbursements tested was accompanied by a disbursement authorization form which was missing a required signature. Additionally, backup documentation was not available for one of our tested disbursements.

Recommendation

We recommend that all disbursements be accompanied by signed disbursement approval documentation, as required by the District's purchasing policy. We also recommend that supporting documentation be attached to all disbursements.

Management's Response

As noted above, significant improvement has been made in this area, as the auditors found only one exception where a disbursement was made without a properly signed request form. Management is aware of this exception, and is committed to complying with this requirement. With respect to missing documentation, management is aware of this exception, and is committed to maintaining proper supporting documentation for all disbursements.

Finding (prior year recommendation)

We noted during our prior audit that certain checks ran in error were not always voided properly. Many of these were filed with the voided checks, but they were never "stamped" void. A risk exists that these checks could actually be disbursed fraudulently or by mistake. During the current year, we noted that although voided checks were being bound and retained, they were not being filed in a systematic manner, and certain voided checks could not be located. We noted no additional voided checks that were not properly "stamped" void.

Recommendation

We recommend that all voided checks be systematically filed to ensure that they are properly retained and accounted for.

Management's Response

The District is aware of the voided checks that cannot be located, and is committed to ensuring that all checks are retained and filed in a systematic manner.

STATUS OF PRIOR YEAR RECOMMENDATIONS WHICH HAVE BEEN APPROPRIATELY ADDRESSED BY MANAGEMENT

CASH RECEIPTS

Finding

We noted during our prior audit certain unexplained shortages with respect to daily deposits. In certain cases, deposit tickets were not being used, and at times, deposits were being dropped off at the bank without obtaining a validated deposit ticket.

Recommendation

We recommended that all cash receipts be reconciled, reviewed, and deposited daily, and that validated deposit tickets be obtained from the bank at the time of deposit. We recommended that deposit slips be used for all deposits, and that a cut-off be established during the day so that deposits can be completed before bank closing hours. We recommended that pre-numbered plastic deposit bags be used and sealed to avoid any tampering from the time deposits are reconciled to the time of bank processing. We also recommended that mail be opened and stamped "received" with a dated stamp.

Status

The District has modified its cash receipting and deposit procedures and now reconciles cash receipts daily. The District has also obtained a validated deposit ticket at the time of each deposit.

The District has also implemented a procedure for ensuring the accuracy of all deposits, which are accompanied by a deposit slip and placed in a locked deposit bag.

Finding

We noted during our prior audit that the night cash drop box is not being locked on a regular basis.

Recommendation

We recommended that controls be placed on the drop box to maintain the integrity of the cash receipting process.

Status

The District has installed a new locked drop box for receiving payments. The existing drop box is still in use, and is now being locked regularly.

WATER RESOURCE LOAN PROCEEDS

Finding

We noted during our prior audit that signed copies of draw requests were not always being retained in the District's files.

Recommendation

We recommended that signed copies of draw requests be retained in the District's files.

Status

All draw requests were approved and a copy has been kept in the file. Previous to this recommendation, some of the requests were copied and filed before the authorized signatures were obtained. Signatures are now being obtained before the District's copy is placed into the file.

IMPACT FEES

Finding

We noted during our prior audit that the impact fee ledger account at year end did not include funds that had not yet been transferred, or amounts that were under-funded as of December 31, 2004.

Recommendation

We recommended that all impact fees be transferred to restricted ledger accounts by year end.

Status

All collected impact fees have been transferred to restricted ledger accounts by December 31st.

Finding

We also noted during our prior audit that interest earned from impact fees was not being separately tracked on the impact fee roll-forward schedule.

Recommendation

We recommended that interest be separately identified on the impact fee roll-forward schedule, and that yearly collections be reconciled to the respective general ledger revenue accounts.

Status

Previous to this recommendation, Interest had been tracked separately, just not recorded as a separate line item on the impact fee roll-forward schedule. The District's staff has revised the roll-forward to show the interest as a separate line item beginning for fiscal year 2005. Reconciliation has been done between the respective general ledger revenue accounts.

CASH DISBURSEMENTS

Finding

During our prior audit, we noted that certain checks were allowed to clear the bank with one signature. The purchasing policy requires two signatures on all disbursements.

Recommendation

We recommended that review and monitoring procedures be established to ensure that no checks be issued until two signatures have been obtained.

Status

The District has complied.

Finding

We noted during our prior audit that certain checks were co-signed by the payee.

Recommendation

We recommended that when a check is issued to an individual who has check signing authority that the individual not be a co-signor on the check.

Status

The District has complied.

Finding

We noted during our prior audit that an accounts payable clerk was still listed on the bank's signature card.

Recommendation

We recommended that anyone processing accounts payable not be listed on the bank signature card.

Status

The District has changed the signature cards and is now compliant.

Finding

We noted during our prior audit that, in certain cases, the pre-printed numbers on checks did not agree with the check numbers generated by Caselle.

Recommendation

We recommended that all checks be reviewed carefully before signing and disbursement, and that all check numbers agree.

Status

The District has complied.

Finding

We noted during our prior audit that blank checks were not being locked up.

Recommendation

We recommended that all blank checks be stored under lock and key.

Status

The District has complied.

OTHER CASH ISSUES

Petty Cash

Finding

We noted during our prior audit that several disbursements had no signed approvals in the petty cash log, and many disbursements had no provided description or purpose for the use of funds. We also noted that at least three individuals had access to petty cash during 2004.

Recommendation

We recommended that all petty cash disbursements be logged with proper approvals and descriptions for purpose of use. We also recommended that one primary person (other than the controller) maintain physical custody of petty cash, with the controller approving petty cash disbursements.

Status

The District has installed a new locked security system within the vault for petty cash handling. Access is limited to two employees. The controller no longer has access to petty cash.

Physical Controls

Finding

We noted during our prior audit that certain field crew had access to the office areas where physical cash is held, including petty cash and tills. Cash tills were rarely locked, and the vault where petty cash is stored was open during daytime hours.

Recommendation

We recommended that management limit access to areas where cash is held. We recommended that physical controls be placed upon the tills during daytime hours, to the extent practical.

Status

The main business office has been limited to only office personnel. Separate cash tills with locking drawers have been installed at the counter and in the vault. Each employee has their own key for tills and drawers.

Transaction Dates

Finding

We noted during our prior audit that in certain cases deposits in transit on the impact fee account are taking longer than expected to clear, which leads us to believe that certain transactions are being back posted.

Recommendation

We recommended that all transaction dates properly reflect the actual date that transactions are initiated.

Status

The district has complied.

Employee Advances

Finding

We noted during our prior audit that certain employee advances were not accounted for on the books, and that no formal re-payment schedule had been established.

Recommendation

We recommended that all employee advances be booked as a receivable, and that re-payment schedules be established to ensure prompt re-payment.

Status

The District has complied and has eliminated employee advances.

INVENTORY

Finding

We noted during our prior audit that inventory was not being tracked on any type of inventory management system. Although physical counts are being conducted annually, and costs are being updated by the shop manager every few years, all counts are tracked and adjusted by hand.

Recommendation

We recommended that the board consider an inventory management system.

Status

The District has purchased an inventory management system, and plans to install and implement the system in 2006.

PAYROLL

Finding

We noted during our prior audit that check sequences relating to direct deposit payroll disbursements were not used consistently, making it difficult to track payroll disbursements.

Recommendation

We recommended that management consider alternative approaches to recording direct deposit payroll disbursements in order to achieve more meaningful reporting.

Status

The District now uses a totally different check sequence to record the direct deposit payroll disbursements.

SEGREGATION OF DUTIES AND OVERSIGHT

Finding

We noted during our prior audit that various office staff has been involved with making deposits. We also noted a weakness in physical control and a lack of segregation of duties with respect to billing adjustments.

Recommendation

We recommended if possible that cash receipting and deposits be segregated properly to authorized personnel. We also recommended that employees handling cash be prohibited from making accounting adjustments.

Status

The District has complied with segregating duties relating to cash receipting and deposits. The individuals handling cash have been prohibited from making accounting adjustments.

We sincerely appreciate the cooperation we received from the management and employees of the District during the course of the audit. It has been a pleasure working with them. We appreciate the opportunity to serve as your auditors. If you have any questions regarding any of the matters discussed, please feel free to contact us.

Pinnock, Robbins, Posey & Richins

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